

Superfund Response Action Contractor Indemnification

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SUMMARY: The Environmental Protection Agency (EPA) is issuing final guidelines to implement section 119 of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), as amended by the Superfund Amendments and Reauthorization Act of 1986 (42 U.S.C. 9619) and Public Law 101-584. Section 119 provides the President with discretionary authority to indemnify response action contractors (RACs) for releases of a hazardous substance or pollutant or contaminant arising out of negligence in conducting response action activities at sites on the National Priorities List (NPL) and removal action sites. As delegated by the President, EPA has authority to extend indemnification to RACs working at NPL or removal action sites for EPA, states, political subdivisions of states, federally recognized Indian tribes, and potentially responsible parties (PRPs).

Detailed Summary of Final Guidelines:

Diligent Efforts: To be eligible for indemnification by EPA, a RAC must have made diligent efforts to obtain insurance coverage from non-federal sources. Under a multisite contract, the RAC must agree to continue to make such diligent efforts each time it begins work at a new site.

Prime contracts: For future contracts, EPA does not intend to offer any indemnification unless it did not receive a sufficient number of qualified bids or proposals, and the lack of response can be linked to the absence of indemnification. In such a situation, EPA may issue a new or amended solicitation and offer indemnification. RACs with EPA indemnification coverage under current contracts will be offered coverage under these guidelines. They may negotiate with EPA on the limit and deductible, but the upper limit that they may choose from is determined by the dollar amount of the contract. Coverage of \$75 million is the top limit (with co-payments above \$50 million), and it is available for RACs with contracts of long duration (greater than five years) only. The maximum top limit for other RACs is \$50 million.

A \$15 million aggregate limit per cost-reimbursement contract of long duration (greater than five years) will be added to provide indemnification solely for specialty subcontractors with \$5 million as the maximum amount available on any one subcontract.

Innovative technology RACs: For current contracts and new contracts {pg 5973} where indemnification is offered, the RAC who provides innovative technologies during remedial action (RA) construction may select from a range of limits. However, the deductibles associated

with a specific limit will be lower for these contractors than for other contractors. Eligible RACs may be prime contractors or subcontractors (receiving indemnification from the prime contractor) under fixed-price contracts or subcontractors under cost-reimbursement contracts.

PRP RAC contractors: These RACs will not receive EPA indemnification. SITE Participants and CERCLA 126(g) hazardous workers training grantees: These RACs may be offered indemnification, but the upper limit available to them will be lower than for other RACs. In addition, the deductibles associated with those limits will be lower than for other RACs. Term of coverage: The term of coverage will be ten years.

Surety firms: Firms that provide performance bonds inherit the indemnification agreement of the defaulting RAC if the bond is activated. Renegotiating existing contracts: EPA believes that given the temporary nature of indemnification under its interim guidance (OSWER Directive 9835.5), i.e., the statutory requirement for promulgation of final guidelines subject to public comment, RACs understood that this protection lacked any permanence and was offered on a "claims made" basis. EPA will terminate the contracts of RACs who do not agree to modify the indemnification terms under their existing contracts so that they are consistent with the final guidelines.

I. Introduction

These guidelines meet the statutory requirements of CERCLA section 119(c)(7), which requires the development of guidelines to implement CERCLA Sec. 119 before promulgation of regulations. Since October 1987, EPA has offered indemnification to RACs under an interim guidance, OSWER Directive 9835.5, "EPA Interim Guidance on Indemnification of Superfund Response Action Contractors Under Section 119 of SARA." The interim guidance required a \$100,000 deductible, but it did not state a limit in coverage for the indemnification as required by CERCLA section 119. The interim guidance did not attempt to assess whether indemnification is necessary to encourage RAC participation in the Superfund program, and it assumed that EPA's indemnification is an adequate substitute for insurance.

In the spring of 1989, EPA sent letters to the then-current RACs stating that it had determined that some insurance may be available. The letter instructed the RACs to make diligent efforts to seek insurance from the private sector and forward proof of their diligent efforts to the EPA contracting officer.

On October 31, 1989, EPA published proposed guidelines in the Federal Register (54 FR 46012) and requested public comment. EPA stated that during an information gathering process, it had not been able to gather adequate information to determine the amount of insurance (coverage) that any particular RAC should maintain. EPA further stated that it had not been able to determine the extent to which indemnification should be offered to meet the Agency's objectives, if at all. As stated in the proposal these objectives are:

Provide RACs with a temporary comparable substitute for commercial pollution insurance, in the absence of affordable and adequate commercial insurance coverage or other viable private sector risk transfer mechanisms;

Encourage the insurance industry to provide RACs with adequate and affordable pollution insurance products;

Encourage the development of other private sector mechanisms that provide RACs with adequate and affordable prospective pollution risk transfer mechanisms;

Maintain EPA's fiduciary responsibility to ensure that the Superfund monies are used to clean up sites to the maximum extent possible;

Assure that an adequate pool of qualified RACs will be available to keep the Superfund program operative;

Maintain strong RAC incentives to prevent and reduce RAC induced release incidents throughout a given Superfund response action contract; Maintain strong RAC incentive to continue to seek commercial insurance coverage and/or develop alternative risk transfer mechanisms.

EPA stated that the indemnification limit and deductible scheme should be based on the assumption that the RAC itself is best able to determine its required level of insurance or indemnification coverage. However, EPA believed that the RAC will overstate its required indemnification limit unless a disincentive to overstate is included. Therefore, EPA proposed tying the size of the deductible to the size of the limit.

EPA proposed a "sliding scale" for cost-reimbursement contracts; these are the contracts under which contractors work on EPA-directed tasks on an hourly basis and are reimbursed for costs incurred while performing the work. The contracts are multi-site, with the work at various locations determined after contract award through work assignments issued by EPA. Under the proposal, a RAC could choose a coverage limit it believed it needed up to \$50 million. However, as the limit increased, the deductible would also slide upwards; the deductible paired with a \$50 million limit was \$3.5 million.

For RACs with fixed-price contracts, i.e., Army Corps of Engineer remedial action (RA) contracts, state-lead contracts, and removal site-specific contracts, EPA proposed market incentives to encourage RACs not to request EPA indemnification. That is, EPA would put a value on its indemnification, either as a price charged to the RAC or as an adjustment to a bid reflecting the amount of indemnification requested by a RAC. The General Accounting Office (GAO) in a 1989 report to Congress, "SUPERFUND: Contractors Are Being Too Liberally Indemnified by the Government," recommended that EPA attempt to use the procurement system to see if RACs would work at EPA sites absent indemnification. EPA believed that the use of market incentives to encourage RACs not to ask for EPA indemnification paralleled GAO's recommendation to use the market place to help meet EPA's goals. EPA concurred with the GAO recommendation and believed that this approach would maintain EPA's responsibility to ensure that Superfund monies are used to the maximum extent possible to clean up sites, and at the same time maintain an adequate number of contractors willing to work at EPA sites.

EPA concluded in the proposal that "given the limited data which EPA has had available to it in shaping this scheme, the Agency is particularly interested in receiving further information that may support this or alternative schemes."

EPA received a variety of comments on the proposal; almost all comments were negative. In the summer of 1990, EPA retained a third-party facilitator, Endispute Incorporated, to meet and interview representatives of interested parties to attempt to gain insight into commenters' views. The facilitator met with representatives of EPA, including personnel from the Office of Emergency and Remedial Response, the Office of Waste Programs Enforcement, the Office of General Counsel, and the Office of Policy, Planning, and Evaluation. The {pg 5974} facilitator met with representatives of the Army Corps of Engineers and the Office of Management and Budget. The facilitator also met with representatives of external groups such as trade organizations, RAC interest groups, and the insurance

industry. On February 14, 1991, Endispute presented its report to EPA, "Report on the Results of the EPA-Sponsored Consultation Process on the Proposed Guidance for Section 119 of CERCLA, as Amended." A copy of the report is in the docket for this notice. The report further clarifies the commenters' positions, which are stated in the Response to Comment section of this notice.

In short, commenters asserted that the limits were too low and the deductibles were too high. Most commenters also linked the perceived low limits to a possible negative effect on subcontractors hired by EPA's prime contractors. Most commenters stated that if the prime contractor does not believe that it has adequate coverage, it will not be willing to share any of its indemnification with its subcontractors.

Despite the large number of comments, commenters did not provide additional factual information that would support any specific alternative indemnification scheme. Commenters reiterated the risks that are perceived to be associated with hazardous waste sites. In short, these risks are:

Superfund sites present high risks to people and property.

Remediation technology is new and continually changing. The statute encourages the use of innovative technologies.

Underground work is inherently risky.

EPA, which is subject to community and other socio-political pressures, does not always accept the RAC's recommendation for the best method to clean up the site.

A large majority of commenters recommended an upper indemnification limit of \$200 or \$250 million, but did not present a factual basis for their recommendation. These commenters stated that these higher limits are needed to protect the RAC from a possible catastrophic claim. However, all parties acknowledged that there has been no such claim in the history of the Superfund program. The few potential claims that EPA has received under section 119 or under

the Federal Acquisition Regulation (FAR) indemnification (that preceded Sec. 119 indemnification) have all been relatively small dollar amounts.

Some commenters stated that EPA should not offer indemnification, and that RACs should bear all responsibility for their negligent actions. Inquiries made by EPA have revealed that some RACs are willing to work for other federal agencies, states, and PRPs without indemnification or with very low coverage.

The Agency was, therefore, in the same situation that it was in before the proposal was published; if EPA offers indemnification it must set a limit and a deductible for the indemnification even though little factual data exists on which to base them, or even to determine whether indemnification is needed.

The approach that EPA has decided to take in the final guidelines draws from the first three alternatives outlined in the 1989 FR notice: Provide no indemnification; Provide indemnification subject to statutory requirements; Offer indemnification with market incentives to purchase commercial insurance.

The goal of these guidelines is to ensure that an adequate pool of qualified RACs is willing to work at Superfund sites. This goal must be balanced with EPA's responsibility to protect the financial exposure of the government so that Superfund monies may be used to clean up the maximum number of waste sites. EPA's authority to provide indemnification to RACs for negligent actions is discretionary and is a temporary vehicle. EPA's indemnification authority will only be used to the extent adequate commercial liability insurance is not available.

General Approach

Prime Contracts

For future contracts (or contracts with other agencies or local governments having an inter-agency agreement or cooperative agreement with EPA to clean up Superfund sites), EPA will offer indemnification only if there is a lack of adequate competition for a solicitation due to the absence of indemnification. If this is the case, EPA will offer a new or amended solicitation, and the selected RAC will be eligible for indemnification under these guidelines.

For RACs with fixed-price contracts, EPA proposed in 1989 to use market incentives to encourage RACs not to request indemnification. Under the proposal, RACs would be permitted to determine whether they wanted EPA indemnification and the amount, but their bid would be adjusted higher to reflect the indemnification request. After further consideration, EPA has concluded the proposed adjustment procedure would be unworkable and present considerable obstacles for EPA. EPA decided that, as with new cost-reimbursement RACs, the solicitation process will be used to determine if RACs will work without indemnification.

If EPA offers indemnification to RACs, it still maintains that the RAC is in the best position to know the coverage that it needs. However, to compensate for a RAC's tendency to overstate its needs, EPA will tie the size of the limit with the size of the deductible. These RACs will be able

to choose from a range of limits (and associated deductibles) for the coverage that best meets their needs. The deductible associated with the limit increases as the coverage increases, similar to the scale presented in the 1989 proposal. For the highest level of coverage available for long duration (longer than five years) cost-reimbursement contracts, the RAC must make dollar-for-dollar co-payments for coverage above a certain level. Under this proposal, a RAC will not overstate its needed coverage, and the RAC will retain increasing financial responsibility for smaller claims in proportion to the coverage that it seeks from EPA. EPA believes that the guidelines will promote the development of a private insurance market and encourage RACs to seek alternative coverage from the private sector and permit the private sector to grow absent the need to compete with generous coverage from the federal government. As the RAC community turns to the private sector for coverage, its ability to provide desired products should increase.

EPA believes that it would be in the government's best interest to have the least disruption to the clean-up effort. EPA will negotiate with its RACs to replace their indemnification coverage under the interim guidance with coverage under these guidelines and thereby avoid the need to terminate current contracts. Therefore, EPA will offer modified indemnification agreements with limits and deductibles to RACs and their subcontractors that currently have contracts to perform Superfund work. Since a RAC operating under a current contract will not have to compete in the open market to receive indemnification, EPA cannot use a competitive test to determine if this RAC would work at particular sites without indemnification.

Subcontractors

EPA has tried to address the issue of subcontractor indemnification where the use of subcontractors meets special EPA objectives, such as the use of small and disadvantaged businesses or innovative technologies. In contracts of {pg 5975} long duration (greater than five years), which currently are only the Alternative Remedial Contracting Strategy (ARCS) contracts (regional ten-year contracts for the planning and clean up of CERCLA sites), the prime contractor will have \$15 million (above its own indemnification limit) available to flow down to subcontractors in the subcontracting pool. This pool is generally where small and small and disadvantaged businesses have an opportunity to be involved in Superfund contracting. EPA will also permit RACs, whether they are prime or subcontractors, who provide innovative technologies under a contract to provide remedial action (RA) construction services to obtain indemnification with smaller deductibles than are available to other contractors.

Subcontractors performing remediation work for a cost-reimbursement prime may be eligible to receive additional indemnification for that work. When EPA issues work assignments to prime cost-reimbursement contractors to implement remedial action (RA), the prime contractor is required to initiate the RA through a subcontract (rather than EPA issuing its own solicitation for the work). Under the guidelines, the subcontractor awarded the RA work may be eligible to receive, through the prime contractor, indemnification at the same level of indemnification as contractors hired directly by EPA. However, EPA will require its prime cost-reimbursement contractors to follow the same solicitation procedures as followed by EPA when hiring contractors directly. That is, the prime contractor's original solicitation must not offer indemnification. If there is not an adequate response to the solicitation because of the lack of indemnification, the subcontractors which respond to a new or amended solicitation will be

eligible to receive indemnification through the prime contractor. To receive indemnification, the subcontractor must meet all the requirements of these guidelines, including the diligent efforts requirements.

Length of Coverage

The length of coverage was another area where EPA received a great deal of comment. EPA proposed that it was considering a period of coverage of ten years. Many commenters stated that ten years was too short a period and suggested that EPA adopt a thirty- year period. EPA did consider these requests, but concluded that commenters that argued for a greater length of coverage did not justify a longer term. EPA retained the ten-year period as balance between the need to provide coverage to retain a qualified pool of RACs to work at EPA sites and EPA's responsibility to limit the exposure of the Superfund.

A. Executive Order 12291

Under Executive Order No. 12291, EPA must determine whether a rule is "major" and thus subject to the requirement of a Regulatory Impact analysis. The notice published today is not major because the proposed guidelines will not result in an effect on the economy of \$100 million or more, will not have significant adverse effects on competition, employment, investment, productivity and innovation and will not significantly disrupt domestic or export markets. Therefore, EPA has not prepared a Regulatory Impact Analysis under the Executive Order. The proposed guidelines were submitted to the Office of Management and Budget as required by Executive Order No. 12291.

B. Regulatory Flexibility Act

Whenever an agency is required by law to publish a general notice of proposed rulemaking, the Regulatory Flexibility Act of 1980, 5 U.S.C. 601-612, generally requires that the agency prepare a Regulatory Flexibility Analysis (RFA) describing the impact of the proposed rule on small entities. Because EPA was not required to publish the guidelines as a notice of proposed rulemaking under Sec. 553 of the Administrative Procedure Act (5 U.S.C. 553) or any other law, they are not subject to the RFA requirements of the Regulatory Flexibility Act.
